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**INTRODUCING DEMOCRATIC FINANCIAL INSTITUTIONS
INTO THE LATVIAN AND LITHUANIAN MARKETPLACE
EUR-0023-G-00-2067-00**

World Council of Credit Unions

**Evaluator:
Greg Pirie**

August 16, 1996



WORLD COUNCIL OF CREDIT UNIONS, INC.

August 15, 1996

Melissa Brinkerhoff
AID/ENI/ED/SB
Room 3108
1800 N. Kent St.
Arlington, VA 22209

RE: EUR-0023-G-00-2067-00

Dear Ms. Brinkerhoff:

Please find attached the report of the midterm evaluation of the Latvian and Lithuanian portions of USAID Grant No. EUR-0023-G-2067-00. Greg Pirie, the evaluator, was pleased to receive the comments of the WOCCU Latvia and Lithuania staff, and has requested that we include those comments as part of his report. Please find them at the end of the evaluator's report. Mr. Pirie felt that the comments offered different perspectives and opinions, as well as some updated information which will be valuable to the reader of the report.

Mr. Pirie intended the report to provide constructive recommendations for the remainder of the project. He did not repeat project achievements unnecessarily, feeling that these were well covered in project quarterly reports. We appreciate his candor, and look forward to any comments or questions you may have.

Sincerely,

Bill Dalrymple
Director - European Region

cc: Greg Pirie
Dalia Jurgaityte
Normunds Mizis
Dora Turula
Nelly Mitchell

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**Introducing Democratic Financial Institutions
into the Latvian and Lithuanian Marketplace
EUR-0023-G-00-2067-00**

**Mid-term Evaluation
May-June 1996**

Recommendations

This evaluation has found that the project has generally achieved its planned outputs within the intended time frames. The notable exception to this success is the lower than planned rate of forming Credit Unions in Latvia. This is a result of the new initial capitalisation requirements introduced by legislation in October 1995.

Recommendations made for future strategic directions of the project are:

- Diversifying the source of materials used as resources in the development of training and operational guidance.
- Training project staff to be competent trainers in areas of key importance to Credit Unions.
- Close monitoring of the progress of the Latvian Parliamentary working group's proposals for new Credit Union legislation and attempts to predict the most likely official response. If capitalisation requirements are to be reduced, the future nature of the project's activities must be reconsidered to meet the anticipated demand for operational support services. If predictions suggest the current requirements will not be changed, urgent consideration must be given to the future of the project.
- The level of promotion of the Credit Union concept within Latvia be reconsidered with the intention of maintaining a minimal profile but not increasing the level of awareness or interest in formation of Credit Unions.
- The project vigorously promote the formation of a public service Credit Union amongst Latvian government employees and elected officials.
- The availability of project staff to fulfil a Credit Union support service delivery role be maximised. Both the required skills and the existing skill sets of all staff should be identified and appropriate training commenced. Credit Unions should be allocated to individual staff on a group basis so that a support relationship may be established. Project management practices should develop a peer group approach that relies upon intra-team referral of those support requests requiring a specialised response.
- The continuing identification of new target groups and promotion of the Credit Union concept to those groups be reconsidered, with the intention of reducing the scale of these activities.
- The strategy of early computerisation of new Credit Unions be reconsidered. Investigation of common benchmarks for determining the need for computerisation of an individual Credit Union should be undertaken. Acknowledgment of the attraction of computerisation to Credit Union leadership in the region should be made by introducing debate as to the value of commencing and maintaining Credit

Union operations on a manual system until the agreed upon benchmarks for computerisation are reached.

- Opportunities for internships and accessing resource materials be investigated in Ireland, Poland, and Great Britain. In particular, project staff should be exposed to and participate in the operation of small Credit Unions, field services from Credit Union support organisations, and training activities for Credit Union leadership.
- WOCCU should prepare a comprehensive description of the operating behaviours it requires from the model Credit Union to achieve both the PEARLS standards and to conform to the international statement of Credit Union operating principles.
- WOCCU should produce a coherent statement of the argument in favour of reduced capital requirements for Credit Unions vis a vis cooperative and commercial banks.

Introduction

This paper reports on the mid-term evaluation of the Credit Union development project in Latvia and Lithuania conducted during May and June 1996. The evaluation was undertaken by Greg Pirie, Manager — Member Services, New Zealand Association of Credit Unions.

The project is funded by USAID within the terms of amended project EUR-0023-G-00-2067-00. WOCCU has project management responsibility and is accountable to USAID in respect of the project funding agreements.

The author was selected by WOCCU to undertake the project evaluation on the basis of his independence and experience in the formation and support of new Credit Unions.

The primary objectives of the evaluation are to arrive at an assessment of:

- Receipt of the planned inputs and production of the desired outputs specified in the project's logical framework.
- Accomplishments and/or activities not included in the project design or workplan.
- The project's monitoring and evaluation system.
- Start-up Credit Union activities.
- The strategic issues of significant relevance to the ability of the project to successfully complete all the objectives.

Methodology

Information regarding the current status of the project, in respect of the achievement of planned outcomes, was gathered by (a) review of project proposal and progressive report documents, (b) interviews with in-country and WOCCU project staff, and (c) where possible, observation of specific project activities and outputs.

Consideration of strategic matters drew upon interviews with in-country & WOCCU project staff, representatives of various parties of strategic significance to the project, such as central bankers, political officials, etc, and Credit Union leadership.

A listing of actions undertaken is attached as Appendix A.

Limitations

The evaluation, whilst intended to make judgements about the overall effectiveness of the project, has not been undertaken as an audit of the project's management and administration. Rather, the emphasis has been on identifying the success of the project in accomplishing the intended outcomes, the reasons for any failure to do so, and the relevant strategic issues confronting the project.

Reliance has been placed upon existing progressive reports prepared by both in-country project staff and WOCCU project supervisors. Source verification of some activities — e.g. internship travel to the US — has not been undertaken. Equally, reports of project finances have been accepted without verification.

Some documents were only available to the author in the non-English language in which they were prepared. Reliance was, therefore, placed upon the explanations provided by in-country project staff as to the content of those documents.

Project Objectives

The goal of the project is "...to increase the efficiency of financial markets and to improve the availability of personal financial services to individuals in Latvia and Lithuania, thereby improving the incomes and standards of living for members, their families and their communities."

The purpose of the project is two-fold:

- To create a pool of trained people with the technical and motivational skills necessary to start and manage Credit Unions.
- To promote, organise, and develop financially sound democratic Credit Unions in the two countries.

The intended results of the project are:

- Thirteen operating Credit Unions in Latvia and 15 in Lithuania.
- One Credit Union in each country to act as a model and training centre for the Credit Union management and leadership forming and operating new Credit Unions.
- Transfer of essential democratic processes and appropriate technical skills to the local project staff, key staff within new Credit Unions, and the leadership responsible for continuing the formation of new Credit Unions.
- Credit Union-specific legislation, with appropriate regulations and model by-laws, in both countries that will enable Credit Unions to grow within a regulatory environment that protects members' savings and maximises accountability, safety, and soundness.
- A volunteer based national organisation of Credit Unions in each country, providing representational and operational support services to member Credit Unions.
- Self-regulation by Credit Unions of adherence to recognised standards for prudential operation that will provide a stabilisation function in the event of any Credit Union operating in such a manner as to place members' funds at risk.
- Availability of insurance services for fidelity bonding insurance of Credit Union funds and group life savings and loan protection insurance of members.

Project Performance

It is the author's opinion that almost all project inputs were provided in a timely fashion to both the Latvia and Lithuania projects, and that the outputs of these projects are almost all on target with the exceptions listed below. A summary of project inputs and outputs can be found in Appendix C. It is the author's opinion that the variances in progress to date will have no detrimental impact on the Lithuania project achieving its stated objectives. The future success of the Latvia project will depend largely on the legislative issues currently being addressed by project staff.

Lithuania — Overview

The project has generally met all of the intended outcomes within the planned time frames. The exceptions to this level of performance were:

- For a period of three quarters, project reports indicate a shortfall of one appointment in local project staff. In-country project management was provided for this period by a local project training officer following the departure from the project of the original project manager.

- Not all the planned internships to Poland have been undertaken. This matter is further addressed in this report in the context of future strategies.
- The most recent quarterly progress report (March 1996) anticipates having some four to seven Credit Unions operating. By this date, Vievis Credit Union was actively serving members and the Pakruojis Farmers Credit Union had achieved registration. However, towards the end of the evaluation, confirmation was received of the registration of a further three Credit Unions.

It is the author's opinion that these variances in progress have had no detrimental impact on the project ultimately achieving its stated objectives.

Lithuania — Human Resources

Overall, it is the author's opinion the project is extremely well served by its in-country staff. The development of a high quality professional team has been further enhanced by the appointment of the current project manager. All staff exhibit a high degree of motivation — beyond that of competent employees — to accomplish the project's goals.

Furthermore, all staff have clearly integrated their understanding of the economic and social benefits of a effective Credit Union System into their personal motivation to contribute to the transformation of Lithuanian society.

The skill sets of current staff appear to be more than adequate to meet the requirements of the project's current activities. All staff have demonstrated a high degree of adaptability and skill in intelligently assimilating new information through:

- a) investigating foreign resource materials and example operations of a business concept initially unknown to them;
- b) adapting the core Credit Union model to suit both local regulations and more general conditions;
- c) developing materials that appropriately and correctly communicate the concept, benefits, and operational requirements of Credit Unions to a wide variety of audiences;
- d) assisting those groups wishing to form a Credit Union with the practicalities of preparing a business plan and meeting registration requirements.

Lithuania — Introducing the Credit Union Concept & Training

A major activity of the project since its in-country commencement has been the promotion of the Credit Union concept to groups identified as having the potential to supply the membership of a Credit Union. Initial promotional activities are the beginning of a three level training experience designed by the project to meet the needs of leadership of those groups which choose to form a Credit Union.

The components of the training programme are detailed in Appendix B. The third level specialised training is still in development and has yet to be delivered to any Credit Union. As at 30 April 1996, a total of 734 people had participated in 35 of the introductory promotional training workshops of the project. A further 15 have attended specialised courses in various aspects of financial institution management at the Commercial Bankers' Association.

The primary resources being used by the project are the core training modules developed by WOCCU and a wide range of training and reference materials from CUNA (USA).

|| It was not possible to assess the suitability of the final Lithuanian version of the translated and adapted training materials, reliance being placed on the universality of the WOCCU programme. However, it is recommended the project

access training materials from within those Credit Union Systems with Credit Unions more akin to the experience of Lithuania. Both the Irish and Polish Credit Union Movements should be investigated for this purpose.

In anticipation of the project delivering operational training to Credit Union leadership, management, and staff — as envisaged in the current training plan — it is recommended the relevant project staff be trained to be competent trainers in areas of key importance to Credit Unions: financial management, strategic planning, and services development.

Lithuania — Potential Credit Unions

At the time of evaluation, project staff have identified thirteen groups with a believed potential Credit Union membership of 17,700 people. Of these groups, five have registered and licensed Credit Unions.

Latvia — Overview

The project has met the planned outcomes in all critical areas with the exception of forming new Credit Unions. This appears to be a direct result of the October 1995 legislation governing all credit institutions. The implications of legislative changes are later addressed in this report.

The following variances are identified in progressive project reporting:

- A shortfall of one appointment in local project staff for an extended period. This arose from difficulties in finding a suitable replacement for an unsuitable training officer terminated early in the project.
- Not all the planned internships to Poland have been undertaken. This matter is further addressed in this report in the context of future strategies.

It is the author's opinion that these variances in progress have had no detrimental impact on the project ultimately achieving its stated objectives. However, the matter of the obstacle to Credit Union development created by the current legislation is of significance. This matter is addressed further in this report.

- Legislation uniquely applicable to Credit Unions has not been enacted. The Credit Institutions Act 1995 specifically includes Credit Unions.
- A greater number of US Peace Corps volunteers have been available than originally planned. This is largely a result of the personal contacts between the local Peace Corps office and the project manager.

Latvia — Human Resources

The local project staff represent a skilled and important professional resource of the project. The skill sets of current staff appear to be more than adequate to meet the requirements of the project's current activities, with the exception of defining and monitoring the performance of the model Credit Union and training centre. This question is further addressed in this report.

As in Lithuania, all professional staff have demonstrated a high degree of adaptability and skill in fulfilling the project's initial requirements for promotional & communication activities, preparation of Credit Union training materials, and identifying the regulatory requirements for registration, licensing, and supervision of Credit Unions.

Latvia — Introducing the Credit Union Concept & Training

Training activities by the project have been organised into three areas: promotion of the Credit Union concept, preparation of the required business plan for a proposed Credit Union, and operational training — still in development. These are detailed in Appendix B.

A significant component in the programme developed in Latvia has been the creation of a theoretical model for a Credit Union System of Latvia. The model communicates a coherent statement of the roles and relationships between six elements: legislators, licensing & supervisory authority, Credit Union central finance facility, stabilisation fund, insurance services, and the Credit Union national association.

The theoretical model appears to be an excellent tool for conveying to interested parties a clear concept of what is envisaged and an encapsulation of the intended strategic outcomes of the project.

The primary resources being used to prepare operational training programmes are the modules supplied by WOCCU. In addition, project staff are attempting to identify potential suppliers of specialised financial institution management training from within Latvia. This is proving to be difficult as these resources are limited in number, are in high demand, and, consequently, either unavailable or too expensive.

The stated intent of the project staff is to act primarily in a coordination role in respect of advanced Credit Union management training — identifying suppliers of training services to meet Credit Union needs. Whilst potentially having the advantage of creating a post-project legacy of known and utilised training services, this strategy has the potential weakness of current staff's inability to adequately assess the quality of the training provided by general suppliers.

Subject to broader strategic considerations concerning the future focus of the project in Latvia, it is recommended the relevant training staff be trained to be competent trainers in areas of key importance to Credit Unions: financial management, strategic planning, and services development. This would give staff the skills to ensure they are selecting external trainers capable of properly meeting Credit Unions' needs and also the ability to deliver training in these areas.

Latvia — Additional Outcomes

The development of a spreadsheet model Credit Union business plan is a significant achievement and appears to be an ideal tool to assist proposed Credit Unions meet licensing obligations. Furthermore, the availability of a standard template has provided the foundation for the budget modelling element of a Credit Union's on-going financial management.

Whilst prepared primarily to support the project's arguments in favour of unique Credit Union legislation, the investigation into the potential for Credit Unions to contribute to the country's economy generally and, more specifically, to improve the standard of living of participating members may provide a useful model for similar exercises in other countries.

Undertaken by a private consultancy staffed by former employees of the Ministry of Finance, the investigation reviews the current economic position of Latvia, examines the causes & consequences of the 1995 banking crisis, and attempts to quantify the economic impact of a strong Credit Union System.

Unfortunately an English version of the report was not available at the time of this evaluation but is expected to be complete by 30 June.

Latvia — Potential Credit Unions

Project staff report a total of seven organisations are in the process of preparing business plans as part of the documentation required by central bank licensing procedures.

These groups include trade unions, small community municipalities, and agricultural business concerns. In total they represent an estimated 44,800 people.

A further seven organisations, with an unknown number of members but each representing more than 1,000 people, are considered by project staff to be serious potential Credit Unions.

Strategic Issues

Latvia

Legislative developments appear to have created a significant obstacle to the formation of new Credit Unions with, therefore, consequential implications for the project.

Credit Institutions Act

Following the crisis amongst commercial banks during 1995, the Government introduced new legislation to regulate the activities and provide for the supervision of all organisations providing credit services. The Act specifies these as including banks, Credit Unions, and branches of foreign banks.

In addition to requiring such entities to generally be registered and to have a specific license from the central bank, the Act introduces a minimum "foundation fixed capital" almost seven times greater than that previously required. The amount set for Credit Unions is specified as ECU50,000.

Currently converting to some LVL34,000 (US\$68,000), this amount equates to 340 times the average monthly nett wage. Thus, the minimum 20 members required to register a Credit Union will have to each contribute the equivalent of 17 months average nett income.

In January 1996 the in-country project staff took the initiative of forming a support group of elected officials to address the need for legislative change for Credit Unions. This group represents a majority of political parties currently in parliament.

Proposals for a specific Credit Union Act were delivered to the central bank for its review and comment in late May. The critical elements in these proposals include:

- A separate statute that removes Credit Unions from the application of the Credit Institutions Act 1995.
- A nil requirement for share capital in order for a new Credit Union to be registered and licensed.
- A minimum capital adequacy level of the equivalent of 10% of liquid assets (including loans to members) to be achieved within five years of commencing operation. It has not been specified if this should be comprised of share capital or balance sheet reserves.
- The mandatory submission by all Credit Unions to the authority of a supervisory regulator empowered to intervene in the affairs of a Credit Union.

The proposals have not specified if such an agency is to be a new Credit Union-specific authority. Initially it is expected to be the central bank.

Assuming agreement with the bank on the content of the proposed law, the draft will be submitted to Latvia's parliamentary process. The best local estimate of the pace at which the draft Act will proceed is that it will be effective prior to 31 December 1996.

This is the project's target date in order to avoid the first increase (1 January 1997) in required capital provided for by the transitional provisions of the Credit Institutions Act.

Without an opportunity to meet with central bank officials, it is difficult to form a judgement as to the likelihood of the bank supporting a separate Credit Union statute, especially with reduced capitalisation requirements. The FDIC

consultant currently providing advice to the central bank in respect of managing the rehabilitation of failing banks expressed the view the central bank would be most unlikely to support any reduction in capital requirements for Credit Unions. When considered within the context of the severity of the banking crisis — which is still being manifested by the placing of further restrictions on some commercial banks as recently as early June — this appears to be a reasonable opinion.

In-country project management has suggested the parliamentary working group is likely to place the draft Credit Union Act before the Parliament even without the support of the central bank. It is believed there is sufficient cross-party support for Credit Union legislation to ensure its passage through the enactment process.

Central Bank Relationship

In the event the central bank declines to support proposals for new legislation and an attempt is made to use purely political processes to achieve a reduction in imposed capital requirements, the possible consequences for the working relationship between the project, central bank, and the Credit Unions it supervises must be considered.

Already the bank has expressed the view there are insufficient Credit Unions to justify it placing any greater emphasis on staff training in the examination and assessment of Credit Union operations. Again, when considered within the context of the scale of the banking crisis such a position is understandable.

Careful consideration must be given to the risk — and consequences — of antagonising the central bank, which is likely to remain the agency with statutory authority for empowering, supervising, and terminating the operation of Credit Unions.

Ministry of Agriculture

It is reported by project staff the Ministry of Agriculture is seeking the inclusion in its next annual budget sufficient funds to meet the initial capital requirements of a relatively large number of Credit Unions. The Ministry apparently intends to support the formation of Credit Unions in rural areas as a means of promoting the agricultural production transformation process. The potential number of Credit Unions is one in each of 26 *pagasts* — the basic administrative unit.

It is not clear how the Ministry intends to make the funds available in a form that meets the statutory limitation for share capital to be owned by individual members of the proposed Credit Union.

However, the primary implication for the project is that of having a large number of Credit Unions formed outside the influence of the project, potentially creating a conflict in the essential operational models adopted by the two agencies.

Implications

The possible scenarios arising from the project's attempt to ameliorate the impact of the new legislation raise serious questions about how the project should continue.

In the event the project is successful in reducing initial capitalisation requirements, it seems highly likely there will be a relatively rapid pace of formation of new Credit Unions commencing in early 1997. Not only will this create issues of operational support for new Credit Unions (see below) but also in respect of the project's termination in September 1997.

The worst case risk is to have a number of Credit Unions formed and commencing operations — perhaps eight to 15 — less than six months prior to closure of the project. It is not unreasonable to expect some of these Credit Unions to fail within the succeeding twelve months, potentially seriously eroding credibility of the Credit Union concept in the region.

A hostile posture of the central bank towards Credit Unions is most likely to increase the probability of the bank taking punitive action against any Credit Unions that breach its requirements. In other words, the bank may choose to adopt a strategy of closure rather than rehabilitation.

In the event the existing legislation remains unchanged, the possibilities for formation of new Credit Unions will be severely curtailed. Under these circumstances it will become difficult to sustain the rationale behind the project.

It is recommended that the progress of the Parliamentary working group's proposals be closely monitored. Commencing with the response of the central bank, attempts should be made at the earliest possible opportunity to predict the most likely official response.

Should such predictions indicate the initial capitalisation requirements are to be reduced, urgent consideration must be given to the future nature of the project's activities with a view towards entering into a suitable strategic alliance with another agency that may be able to meet the anticipated demand for operational support services.

In the event the Ministry of Agriculture obtains the budget allocation it is seeking, this agency should be considered as a potential partner. Consideration should also be given to the potential for an alliance with the EU/PHARE programme within Latvia.

If predictions suggest the current requirements will not be changed, urgent consideration must be given to the future of the project. In either event, it is recommended the level of promotion of the Credit Union concept within Latvia be reconsidered with the intention of maintaining a minimal profile but not increasing the level of awareness or interest in formation of Credit Unions.

A valuable suggestion made by the FDIC adviser to the Bank of Latvia was to investigate the possibility of forming a Credit Union for government employees. She believed this would be advantageous to the project by directly introducing an understanding of the Credit Union concept and experience of Credit Union benefits into the bureaucratic decision-making environment.

It is recommended the project vigorously promote the formation of a public service Credit Union amongst government employees and elected officials.

Credit Union Operational Support

The success of the project in introducing the Credit Union concept to a number of groups which have responded enthusiastically with formation plans, raises a number of questions relating to how those Credit Unions will be adequately supported following their start-up.

Whilst a degree of uncertainty now exists in Latvia, the introduction of applicable legislation and the increasing familiarity of all parties — project staff, each new Credit Union's founders, central bank staff — with the processes for licensing and registration of Credit Unions will mean an increase in the pace of formations in both countries.

It appears reasonable to expect, therefore, increasing demand for such support services as:

- Education & training in the practical realities of Credit Union governance, management, and operation.
- Conversion from initial manual accounting systems to computerised equivalents.
- Problem-solving — operations, policy development & implementation, governance processes, financial management, and development of services.

- Compliance with accounting standards, regulatory reporting requirements, and broader applicable law (credit contracts, tax, employment).

The strategic question for the project is whether or not it should assume a direct responsibility for providing operational support to Credit Unions. Note: The distinction is made between ensuring Credit Union leadership and management are trained and being a subsequent supplier of practical operational support services.

The project plan provides for training of volunteer directors in their duties & responsibilities, and the training of Credit Union managers & staff to carry out financial analysis, liquidity management, capitalisation requirements, risk analysis & management, loan procedures, reserves accumulation, and low-cost computerisation. This training is intended to be delivered primarily by the Credit Union intern programme and in-country activities conducted by a range of suppliers (refer to Annex D *Training Strategy* of the project proposal).

An inevitable consequence of project staff directly undertaking any training will be the expectation by Credit Union staff they can obtain subsequent operational assistance from those who trained them.

Whether for the purpose of meeting Credit Union expectations arising from the delivery of training or for explicitly acting as a supplier of operational support services (or both), it is recommended the availability of project staff to fulfil support service delivery role be maximised. This will require a combination of managing individual job orientation & priorities and the acquisition of the necessary skills by staff. Both the required skills and the existing skill sets of all staff should be identified and appropriate training commenced.

In general terms, all staff should have the ability to provide Credit Unions with broad operational advice, including the competence to recognise when any particular request for assistance should be referred to the person most able to assist. The role may be generally considered as being equivalent to that of a 'field worker' in the early development of the national associations of the now mature Credit Union systems.

Skill sets that should be considered as universally desirable amongst all staff include:

- Credit Union bookkeeping to trial balance level.
- Working knowledge of the application of critical elements of the Credit Union law.
- Knowledge of which non-Credit Union specific statutes apply to various aspects of Credit Union operation.
- Fundamentals of Board governance functions (meeting procedure, record-keeping, role of policy, management reporting).
- Use of standardised documentation (e.g. loan processing)

Consideration should be given to allocating Credit Unions to individual staff on a group basis so that a support relationship may be established. This should not limit the provision of support to any one Credit Union by the allocated staff member. Project management practices should develop a peer group approach that relies upon intra-team referral of those support requests requiring a specialised response.

It is further recommended that the continuing identification of new target groups and promotion of the Credit Union concept to those groups be reconsidered, with the intention of reducing the scale of these activities. In other words, an appropriate balance must be struck between the need to maintain the momentum of emerging interest in the formation of Credit Unions, and the ability of the project to meet the needs of those seeking its support.

Computerisation Strategy

Inherent in the project is the provision of computerised accounting systems for the Credit Unions formed as a result of the project's activities. The software system *Microbanker* has been adopted by both the project for Latvia and Lithuania and by the Credit Union development activities of the Desjardins group in Lithuania.

An initial, albeit superficial, observation of *Microbanker* suggests it will generally meet the needs of Credit Unions in those countries.

However, the author questions the emphasis being placed on the early conversion of Credit Unions from manual to computerised accounting systems. Experience with the extensive support of Credit Unions from their beginnings through subsequent growth and computerisation suggests there are important advantages to be gained from having successfully managed a manual accounting system prior to computerisation.

Competence in correctly maintaining an up-to-date manual system, which is successfully reconciled internally and externally, establishes skills vital to the correct operation of a computerised equivalent. The labour intensive requirements of identifying and correcting the source of any error in a manual system, working within the linear processes of that system, require the understanding of the underlying logic applicable to any accounting system.

Without such an understanding, the ability of the operator of an accounting system to correctly identify the source of an accounting error and, more importantly, to determine the most appropriate correction tactic, is extremely limited.

In the absence of a high level of self-sufficiency amongst Credit Union staff in this area, the need for a strong external operational support service will be intensified. Relatively unskilled dependency upon technology creates a matching dependency upon suppliers of support services. In an environment where the availability, quality, and cost of those services cannot be assumed, the risks for Credit Union operation are significant.

It is recommended the strategy of early computerisation of new Credit Unions be reconsidered. Investigation of common benchmarks for determining the need for computerisation of an individual Credit Union should be undertaken. These may relate to membership numbers, transaction volumes, asset size, etc. Acknowledgment of the attraction of computerisation to Credit Union leadership in the region should be made by introducing debate as to the value of commencing and maintaining Credit Union operations on a manual system until the agreed upon benchmarks for computerisation are reached.

Resources & Internships

The predominant source of internship opportunities for both project staff and Credit Union leadership has been the USA. Much of the training and operational guidance material available to project staff has been developed within the US Credit Union Movement.

Whilst the US Movement has the advantage of a highly developed resource base and a wide range of Credit Union experience amongst a large number of people, it has a relatively small number of Credit Unions still in the early days of the post-formation experience. Equally, the maturity of the US Movement is such that start-ups of new Credit Unions are relatively infrequent events.

It is, therefore, the author's view that, in addition to the US, Latvian and Lithuanian project staff and Credit Union leadership should be exposed to Credit Union Systems in countries where supporting simpler and newer Credit Unions is a more general experience.

It is recommended opportunities for internships and accessing resource materials be investigated in Ireland, Poland, and Great Britain. In particular, project staff should be exposed to and participate in the operation of small Credit Unions, field services from Credit Union support organisations, and training activities for Credit Union leadership.

Model Credit Union & Training Centre

A critical component in the project is the creation of a model Credit Union and associated training centre. The purpose of these project outcomes is to provide a post-project resource for the continuing training of Credit Union leadership and staff as the momentum of Credit Union formation proceeds.

The role of the model Credit Union and training centre is, therefore, of major strategic importance to the project. In Latvia the Railroad Credit Union has been designated the model Credit Union and has entered into a contractual agreement — in the form of a memorandum of understanding — with the project regarding its role and the operation of a training centre in the Credit Union's premises. No equivalent yet exists in Lithuania.

It is of considerable value to have a contractual relationship that provides for the Credit Union to have its personnel trained by WOCCU, to follow model Credit Union PEARLS operational standards, and work according to a mutually agreed work plan.

However, there does not yet appear to be any statement of the operating behaviours of the Credit Union that will be considered acceptable to the project. It is insufficient to rely exclusively upon the Credit Union achieving the prudential results prescribed by PEARLS.

For example, PEARLS requires a minimum level of operating profit to contribute to the creation of healthy balance sheet reserves. Is it acceptable for such a result to be achieved by consistently charging interest rates on loans two or three times the market rate? For many Credit Unions their members have few choices and, therefore, are something of a 'captive market'. In such circumstances the pressure of market forces to prevent usury is ineffective. Will it be acceptable for the model Credit Union to behave in a manner contrary to generally accepted standards of Credit Union operation even if it satisfactorily achieves the PEARLS outcomes?

It is recommended WOCCU prepare a comprehensive description of the operating behaviours it requires from the model Credit Union to achieve both the PEARLS standards and to conform to the international statement of Credit Union operating principles. This description should form the basis for the work plan to be mutually agreed upon within the terms of the memorandum of understanding.

This description should also form the basis of the key outcomes expected from the operation of the training centre, i.e. participants in the centre's training activities will leave with a clear understanding of both the PEARLS standards, the international operating principles, and the desired methodologies for achieving these.

Regulatory Environment

In February 1995 the Lithuanian Parliament adopted a Credit Union-specific statute that comprehensively provides for the organisation, incorporation, registration & licensing of Credit Unions, their governance & organisational structure, supervision, liquidation, and various aspects of their operation.

The Act has been critically reviewed for WOCCU by external consultant Alfredo Lanza-Cuellar.

In October 1995 the Latvian Parliament adopted the Credit Institutions Act with explicit application to Credit Unions (see above). The matter of this Act's capitalisation requirements has been critically reviewed for WOCCU by external consultant Alfredo Lanza-Cuellar.

Thus, the project has achieved its intended objective of Credit Union-specific legislation in both countries. Whilst Latvian legislation is a subset of a broader Act, the specific recognition of Credit Unions has advantages over using an otherwise inappropriate statute (such as friendly societies, provident societies, etc).

In both countries concern was expressed about the capital requirements for registering and licensing Credit Unions. The Lithuanian Credit Union Act requires a minimum of LTL15,000 (US\$3,750). This did not appear to be an obstacle to the formation of the five Credit Unions registered to date. However, even the Chair of the Parliamentary Finance & Budget Committee expressed the view it was hindering the formation of Credit Unions, especially those in rural areas, and requested financial assistance from the US for this purpose.

The implications of the Latvian Credit Institutions Act have been addressed above.

It is reasonable to expect the capital requirements of the Lithuanian Credit Union Act may be subject to revision if the Lithuanian government believes it is necessary to make changes as part of their bid for membership of the EU. If this occurs, the same concerns as currently exist in Latvia may also apply here.

It is recommended WOCCU familiarise itself with the initiative of the Irish and British Credit Union Movements to obtain appropriate specific recognition of Credit Unions within relevant EU directives concerning financial institutions. The extent to which the emerging Credit Union Systems in Central & Eastern Europe can support this initiative, either by direct action or through their political representatives, should be investigated as many of those states are seeking membership of the EU.

It is recommended WOCCU produce a coherent statement of the argument in favour of reduced capital requirements for Credit Unions vis a vis cooperative and commercial banks. It must be recognised that to the disinterested consideration of central bankers and government officials responding to the poor performance of many of the region's commercial banks the argument that Credit Union members somehow are prepared to assume a greater level of risk than that of bank customers is unlikely to be attractive.

G. J. Pirie
14 June, 1996

GREG PIRIE

Achievements:

- **Provided full support in the formation of fourteen Credit Unions.**
- **Primary trouble-shooter for all operational/accounting problems.**
- **Converted 23 Credit Unions to or between computerised accounting systems.**
- **Developed, trained, and managed Consultancy Services team to meet prudential standards, operational advice, education & training, and marketing support requirements of Credit Unions.**
- **Supervised and guided development of NZ's first comprehensive Credit Union training programme.**
- **Designed and implemented NZ's first computerised Credit Union statistical database and performance monitoring system.**
- **Designed and conducted NZ's first universal actuarial risk assessment.**
- **Represented Credit Unions to the Securities Commission during liaison for preparation of prospectus regulations (statutory public disclosure document).**
- **Maintained model prospectus and associated guidelines for use by Credit Unions with Dept of Justice.**
- **Supervised and guided accounting advisers' (Price Waterhouse) preparation of financial reporting models and manual.**
- **Supervised and guided accounting advisers' (Price Waterhouse) preparation of guide for Credit Union auditors in association with NZ Society of Accountants.**
- **Conducted Credit Union fraud investigations.**
- **Assisted Dept of Justice investigations (S67 Securities Act).**
- **Controlled the liquidation/merger of 43 Credit Unions.**
- **Provided the definitive interpretation of merger provisions of the Friendly Societies & Credit Unions Act adopted by the Registrar of Friendly Societies & Credit Unions.**
- **Researched and introduced the savings protection fund concept to NZ.**
- **Prepared analytical summaries of proposed taxation, proceeds of crime, and money laundering legislation.**
- **Facilitated strategic planning for 27 Credit Unions.**
- **Extensive training of Credit Union volunteers and staff in all aspects of core operations.**

Experience:	<p>New Zealand Association of Credit Unions:</p> <ul style="list-style-type: none"> • 1993 - Present Manager — Member Services • 1988 - 1993 Manager — Consultancy & Special Services • 1984 - 1988 Senior Consultant • 1982 - 1984 Field Officer <p>Previously:</p> <ul style="list-style-type: none"> • Social research (Citizens' Advice Bureaux), international aid & development education (CORSO), ambulance service. 												
Education:	<ul style="list-style-type: none"> • Credit Union Development Education course, Credit Union Foundation Australia 1995. • Te Ataarangi Purapura (Maori language) course, Waikato Polytechnic 1992. • Management Skills course, NZ Association of Credit Unions 1991. • Management Programme, University of Auckland Graduate School of Business 1990. • Credit Union Financial Management Course, Australian Institute of Credit Union Management 1987. • BA Degree (Educational Psychology), University of Auckland 1980. 												
Publications:	<p>"Reality in New Zealand's 'land of plenty'", <i>Perception</i>, Vol. 19, No. 1, Fall 1995, Canadian Council on Social Development.</p> <p><i>Audit Guide for Credit Unions</i>, with M. Hucklesby BCA (Hons), ACA, February 1994, NZ Society of Accountants.</p> <p>"Credit Unions — Unique Challenges for Auditors", with M. Hucklesby BCA (Hons), ACA, <i>Accountants' Journal</i>, Vol. 73, No. 1, February 1994.</p> <p><i>Financial Reporting Guidance Manual</i>, with M. Hucklesby BCA (Hons), ACA, March 1993, NZACU.</p> <p><i>A Self-Regulatory Regime for New Zealand's Credit Union Industry</i>, March 1993, NZACU.</p> <p>"Credit Unions and the 'Free Market'", <i>The Employment Catalyst</i>, Vol. 2, December 1992.</p> <p>"A Change Of Direction — New Zealand's Stabilisation Fund", <i>World Reporter</i>, September 1991, WOCCU.</p> <p><i>Operating guides:</i></p> <table border="0"> <tr> <td>• Unclaimed Moneys Act</td><td>• Resident Withholding Tax</td></tr> <tr> <td>• Mergers (Statutory Requirements & Accounting)</td><td>• Association Dues</td></tr> <tr> <td>• Travellers Cheques</td><td>• Investment of Surplus Funds</td></tr> <tr> <td>• Prospectus</td><td>• Repossession of Chattels</td></tr> <tr> <td>• Line of Credit Lending</td><td>• Auditor's Report</td></tr> <tr> <td></td><td>• Dissolution Procedures</td></tr> </table>	• Unclaimed Moneys Act	• Resident Withholding Tax	• Mergers (Statutory Requirements & Accounting)	• Association Dues	• Travellers Cheques	• Investment of Surplus Funds	• Prospectus	• Repossession of Chattels	• Line of Credit Lending	• Auditor's Report		• Dissolution Procedures
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• Travellers Cheques	• Investment of Surplus Funds												
• Prospectus	• Repossession of Chattels												
• Line of Credit Lending	• Auditor's Report												
	• Dissolution Procedures												

Appendix A

LITHUANIA

Actions Taken	Documents Reviewed
<p>Interviews with project staff:</p> <p>general overview — all staff</p> <p>training activities — Regina Laimikiene (Training Officer) & Natalija Firsova (Training Officer)</p> <p><i>Microbanker</i> Credit Union accounting software — Vytautas Latinas (Computerisation Specialist)</p> <p>project administration & accounting — Lina Bulotaite (Administrative Assistant)</p> <p>aspects of Credit Union law and regulatory requirements — Gediminas Reciunas (Legal Adviser)</p> <p>project performance & strategic direction — Dalia Jurgaityte (Credit Union Development Specialist)</p>	<p>project proposal</p> <p>monthly & quarterly project reports October 1994 — February 1996</p> <p>project achievement summary April 1996</p> <p>Credit Union Act</p> <p>consultancy evaluation of Credit Union Act</p> <p>Confirmation Order of Licenses for Credit Unions Issue and Cancellation</p>
<p>Parliamentary Finance & Budget Committee liaison — Mr Kolosauskas (Chair) and two others</p>	<p>training programme structure</p> <p>training participation statistics</p>
<p>SDID liaison — Yves Boily (Programme Officer) & Regina Piecaitis (Project Director)</p>	<p>standard chart of accounts</p>
<p>World Bank liaison — Ramune Zabuliene (Branch Manager)</p>	<p>Vievis Credit Union trial balance 31 March 96</p>
<p>USAID liaison — Rasa Ciceniene (Project Management Specialist)</p>	<p>media reports on Credit Unions</p>
<p>Visit Vievis poultry factory Credit Union</p>	<p>local office work plan 1996</p> <p>identified potential Credit Unions</p>
<p>President's Office liaison — Raimundas Duzinskas (Adviser on Agricultural Affairs & Rural Development)</p>	<p>cooperation contract</p>
<p>Social Democratic Party liaison — Aloyzas Sakalas (Party Chair & Parliamentary Vice-Chair) and three others</p>	
<p>Centre Party liaison — Egidijus Bickauskas (Parliamentary Vice-Chair)</p>	
<p>Local Authorities Association liaison — Alfonsas Brazas (Programme Director)</p>	

Central Bank liaison — Audrius Misevicius (Deputy Chair), Jurate Mackeviciute (Manager of Licensing Division), & Gintautas Juknevičius (Deputy Director — Supervision)

LATVIA

Actions Taken	Documents Reviewed
<p>Interviews with project staff:</p> <p>general overview — all staff</p> <p>current project status (particularly legislation) — Normunds Mizis (Project Manager)</p> <p>training activities, resource development, Credit Union potential — Brigita Baltaca (Training Officer), Tatyana Volkova (Training Officer)</p> <p>project performance & strategic direction — all staff</p>	<p>project proposal</p> <p>monthly & quarterly project reports November 1994 — November 1995</p> <p>progress report 31 March 1996</p>
<p>Interview with Kathryn Woolford — USAID adviser to central bank (failed banks specialist)</p>	<p>Credit Institutions Act 1995</p> <p>model Credit Union Rules (November 1993)</p> <p>WOCCU consultancy review of minimum capital requirements of Credit Institutions Act 1995</p>
<p>Interview with Credit Union founders in Cesis region</p>	<p>action plan for development of Credit Unions in Cesis</p>
<p>Interview with Railroad Credit Union manager</p>	<p>local consultancy report on the potential contribution by Credit Unions to general economic development and improvement in participants' standard of living (NB: in Latvian)</p>
<p>attendance at opening of new Railroad Credit Union office and model Credit Union training centre</p>	<p>listing of "initiative groups" representing potential Credit Unions</p>
<p>Interview with USAID project management specialists — Indra Arone & Elita Sproge</p>	<p>theoretical model of a Credit Union System for Latvia</p> <p>table of Latvian Credit Unions 1922-1940</p> <p>training/promotional seminar content summary</p>

Appendix B

Lithuania Credit Union Training Programme

Introduction to Credit Unions

- What is a Credit Union
- History of the Credit Union Movement
- International Operating Principles
- The self-supporting financial Credit Union System
- Organisational structure of a Credit Union
- Credit Unions and other financial institutions
- Lithuanian legal environment for Credit Unions

Main Course

- The economic and financial environment
- Credit Union services
- Structure of a Credit Union
- Duties and responsibilities of structural units
- Sources of capital
- Types of credits (loans to members)
- Forecast of financial activities
- Business plan
- By-laws, licensing, and registration requirements

Specialised Course

- Financial management
- internal controls
- auditing
- computerisation
- Credit Union specific training

Latvia Credit Union Training Programme

Training Sessions

- What is a Credit Union
- History of the Credit Union Movement and development in the world
- Structure and operating principles of a Credit Union
- Strategic planning of Credit Union operations and balance sheet
- Credit policy of a Credit Union
- Credit Committee — duties and responsibilities
- Business plan of a Credit Union

Let's Get Acquainted With Credit Unions

- WOCCU project in Latvia
- What is a Credit Union
- History of the Credit Union Movement and of Credit Cooperatives in Latvia
- Operating principles of a Credit Union
- Self-supporting financial system of Credit Unions
- Organisational structure of a Credit Union
- Credit Unions and other financial organisations
- Legal environment in Latvia. Cooperation with legislators

Business Plan of a Credit Union

- Economic and financial environment
- Field of membership
- Mission statement and objectives
- Credit Union services
- Structure of a Credit Union
- Duties and responsibilities of structural units, management, and staff
- Sources of capital, capitalisation, and deposit services
- Types of credits
- Lending policy
- Administration of lending and loans
- Risk management
- Forecast of financial activities for two years

Appendix C

VII. Project Inputs/Outputs

PROJECT INPUTS	Latvia			
	Year 2 Proposed	Proj/Date Actual	Proj/Date Proposed	Life/Proj Projected
Long-term/short-term Technical Assistance				
Credit Union Development Specialist (Local)	0	1	1	1
Local Project Staff	2	4	4	4
Short-term Consultants (including In-County)	3-4	3	3	6
Internships to USA, Canada, Ireland, etc.				
Local Project Staff	2	4	4	6
Credit Union Interns	4-6	0	0	13*
Internships to Poland	10	1	2	19
VOCA Volunteer Assignments	N/A	N/A	N/A	N/A
IESC Volunteer Assignments	N/A	N/A	N/A	N/A
U.S. Peace Corps Volunteers Promoting CU's	4-8	4	2	10
CU-to-CU Partnership Agreements	1-2	0	1	4
Learning Center Module & National Center				
Computers on Local Area Network	3	6	3	6
Laser Printers	0	1	1	1
Dot Matrix Printers	1	2	1	2
Sets of Training Equip. (copier, modem, fax)	0	1	1	1
Technical Books Translated & Adapted	3	4	4	5

PROJECT OUTPUTS	Latvia			
	Year 2 Proposed	Proj/Date Actual	Proj/Date Proposed	Life/Proj Projected
No. of SCU's	3-5	1	2	13*
No. of SCU's as Mini Learning Centers	1	1	0	1
No. of Members	1500-3000*	526	2000*	13000*
No. of Leaders able to Support CU's	36-60	25	0	156*
SCU Managers Trained	4-6	5	0	13*
New Credit Union Law	1	0	1	1
Enabling Rules and Regulations, By-laws, Policies	1	0	0	1
# of SCU's Applying Democratic Processes	3-5	1	2	13*
# of SCU's w/Loan Prot, Life Sav. & Bond Ins.	0	0	2	13*
# of SCU's Applying App. Oper. Polic. & Proceed.	3-5	1	2	13*
# of SCU's w/Oper. Safe & Sound Pol. & Proc.	3-5	1	2	13*
PC-based Account and Report Software Utilized	3-5	0	0	13*
National Safety & Soundness Committees Set & Monitor				
Financial Standards	0	0	0	1
National Volunteer Association**	0	1	0	1

* will be revised because of reemphasizing project objectives

** is not actively involved in CU development

Appendix C

	Lithuania			
PROJECT INPUTS	Curr. Qtr. Actual	Proj /Date Actual	Proj/ Date Proposed	Life/Proj Projected
Long-term/short-term Technical Assistance				
Credit Union Development Specialist (Local)	0	1	1	1
Local Project Staff	0	3	4	4
Short-term Consultants	0	0	0	6
Internships to USA, Canada, Ireland, etc.				
Local Project Staff	1	5	5	12
Credit Union Interns	0	0	0	15
Internships to Poland	0	3	4	21
VOCA Volunteer Assignments	0	0	0	5
IESC Volunteer Assignments	0	0	0	9
U.S. Peace Corps Volunteers Promoting CU's	0	0	0	10
CU-to-CU Partnership Agreements	0	0	0	4
Learning Center Module & National Center				
Computers on Local Area Network	0	3	3	6
Laser Printers	0	1	1	1
Dot Matrix Printers	0	2	1	2
Sets of Training Equip. (copier, modem, fax)	0	1	1	1
Technical Books Translated & Adapted	0	4	4	5

	Lithuania			
PROJECT OUTPUTS	Curr. Qtr. Actual	Proj/Date Actual	Proj/Date Proposed	Life/ Proj Projected
No. of SCU's	5	5	4-7	15
No. of SCU's as Mini Learning Centers	0	0	0	1
No. of Members	400	400	3000	15000
No. of Leaders able to Support CU's	5	5	4-7	180
SCU Managers Trained	5	5	4-7	15
New Credit Union Law	0	1	1	1
Enabling Rules and Regulations, By-laws, Policies	0	0	0	1
# of SCU's Applying Democratic Processes	5	5	4-7	15
# of SCU's w/Loan Prot. Life Sav. & Bond Ins.	0	0	0	15
# of SCU's Applying App. Oper. Polic. & Proced.	5	5	4-7	15
# of SCU's w/Oper. Safe & Sound Pol. & Proc.	5	5	4-7	15
PC-based Account. and Report Software Utilized	0	0	0	15
National Safety & Soundness Committees Set & Monitor Financial Standards	0	0	0	1
National Volunteer Association	0	0	0	1

Comments on Mid-term Evaluation Report WOCCU/Latvia staff

WOCCU/Latvia staff has introduced themselves to the Mid-term Evaluation Report and have following comments on some of the issues mentioned in the Report:

Page 1 and page 11 of received draft report:

The level of the Credit Union concept within Latvia be reconsidered with the intention of maintaining minimal profile but not increasing the level of awareness or interest in formation of Credit Unions.

After changes in credit union legislation in Latvia and review of project goals by WOCCU European Regional Director, European Regional Project Officer and In-county Project Manager in the context of new Law on Credit Institutions in November 1995, project has reduced activities in promoting formation of new credit unions and is concentrating on improvement of legal environment, building infrastructure to meet training and service needs of newly developed credit unions after the end of WOCCU project and providing appropriate training to the existing initiative groups and working with people who are seriously planning to start a credit union. Such a strategy was discussed with and approved by US AID Country Representative in Latvia in November 1995. Since then in development of new credit unions WOCCU/Latvia staff has been working only with those groups, who approach the Project with request for assistance and training.

Page 2 and page 13

It is recommended that strategy of early computerization of new credit unions be reconsidered.

Project staff feels that computerization is very important element of the success of the project and safety of credit union system. Firstly, if WOCCU will not accomplish this task before the end of the project, developing credit union system may be left without resources and money to invest in such a project, as a result of which credit unions may stay on manual accounting for an extended period of time or will have to increase interest on loans to cover expenses associated with computerization. Manual accounting for a rapidly growing credit union (like RCU in recent months) is very time consuming and may become cost inefficient. Secondly, credit unions may choose to use different software which may be not of the best quality and can potentially impose high costs of software maintenance and/or lead to mismanagement of credit union. Thirdly, local legislation requires that credit union accountants must have appropriate education and prior experience working as accountants and must pass a test in Bank of Latvia as accountants of credit institution. This procedure ensures that those people know basics for accounting and are able to determine problems if books do not balance. Also, training programs on computer software ensure that credit union accountants are able to utilize computers efficiently. At this stage it seems that the most important issue is to agree on the best

methods of computerization of CUs and establishment of software maintenance support center/resource at the end of the project.

Page 2 and page 14

It is recommended WOCCU prepare a comprehensive description of operating behaviors it requires from the model credit union to achieve both the PEARLS standards and to conform to the international statement of credit union operating principles. ...

Does not Model Credit Union Handbook answer this question? It was distributed at the Project Advisor Workshop in April 1995 and is currently available in Latvian as well.

Page 7

The stated intent of the project staff is to act primarily in coordination role - identifying suppliers of training services to meet Credit Union needs.

WOCCU/Latvia Project staff is fully equipped to provide Level I training (Levels of training are discussed in details in Project Proposal) and Level II training materials and methodology will be developed in full by the end of the year. Level III training requires assistance of consultants from outside of the Project. After such consultancies Project Trainers will be able to further provide training themselves (e.g. strategic planning, conversion from manual accounting to computerized one, etc.). However, there will be areas in which not only staff training but also appropriate background and experience is required (e.g. accounting, financial analysis and troubleshooting, etc.). Since our staff currently does not possess some of these qualifications we need to ensure that people with appropriate backgrounds are trained and will be available to project staff and credit unions once the need arises. Therefore it is not our intent to act primarily as coordinators but, instead, to use our skills as efficiently as possible and involve outside experts in cases when specific experience and backgrounds are required.

Page 8

The amount set for credit unions is specified as ECU50,000 and mirrors requirements within EU for cooperative banks.

In our discussions with Bank of Latvia representatives the issue of the origin of this amount has been raised several times. They have made comments that it is a requirement of EU for credit unions but always failed to provide us with the source of information on such a requirement. Two credit union movements existing within EU are in Ireland and Great Britain and are operating in the EU financial market under exemption, so no centralized regulations exist for them. Also, from the EU documents and directives which are at our disposal we could not identify the source of such a statutory capital requirements. In case you have any of such documents we will highly appreciate if we could obtain a copy of them.

Page 10

It is reported by project staff the Ministry of Agriculture is seeking the inclusion in its next annual budget sufficient funds to meet the initial capital requirements of a relatively large number of Credit Unions.

After the meeting with State Minister for Cooperation in the Ministry of Agriculture it was determined that there will be no funds allocated from state budget to Ministry of Agriculture for provision of statutory capital to rural credit unions. Instead, there is a possibility that some funds might be made available from Privatization Fund to the Rural Development Fund (subsidiary of Ministry of Agriculture) which then can be lent to credit unions for improvement of cash flow and other purposes. At this point it seems that Ministry of Agriculture officials are pretty realistic in their expectations and if any funds are received for this purpose, they will not become subsidies for farmers distributed through credit unions and will be used for the benefits of CUs. Still number of activities have to be undertaken to ensure that such funds will be used for the benefits of rural credit unions, but at least there are signs of realistic approach to CU development in rural areas demonstrated by Ministry of Agriculture which may lead to efficient cooperation between project and MoA.

The worst case risk is to have a number of Credit Unions formed and commencing operations - perhaps eight to 15 less than six months prior to closure of the project. It is not unreasonable to expect some of these Credit Unions fail within the succeeding twelve months, potentially seriously eroding credibility of the Credit Union concept in the Region.

Taking into account severe banking crisis in summer of last year Bank of Latvia has developed efficient methods for monitoring performance of credit institutions which allow to determine problems in credit institutions before they start threatening the viability of credit union. This comment is to state that system of control and supervision in Latvia exists and provides some guarantee for protection of member savings. Also, after reemphasis on project goals in November 1995 project staff is working to achieve development of credit union support system and increase safety of credit union operations in the future. However, despite to the above stated arguments under circumstances provided in the Report risk of failure for some credit unions may remain relatively high. Credit union's failure may be a significant erosion to credibility of credit union movement in country, but most likely will not have an effect on a credit union development in the region, as failures of credit unions in other countries have had no effect on the development of CUs in Latvia.

A hostile posture of the central bank towards credit unions is most likely to increase the probability of the bank taking punitive against any credit unions that breach its requirements. In other words, bank may chose to adopt a strategy of closure rather than rehabilitation.

Latest comments of central bank official indicate that Bank of Latvia does not have anything against credit unions and would like to transfer supervision and licensing to a different, possibly credit union movement controlled organization. It was also expressed by a member of Board of BoL that comments prepared by Bank of Latvia on draft Credit Union Law are favorable in principal. Copy of the comments is expected to be received from the Parliamentarian who asked for them some time this week.

In the event existing legislation remains unchanged, the possibilities for formation of new credit unions will be severely curtailed. Under these circumstances it will become difficult to sustain the rationale behind the project.

In our opinion WOCCU Project in Latvia is a unique opportunity for the country to set up safe and sound member friendly financial system which is an alternative to the only currently existing financial servicing system in Latvia - commercial banking sector. In case the pace of achieving legal reform is not fast enough, WOCCU should use all the available tools to try to make legal environment for credit unions friendly by the end of the project, otherwise country is running a risk leaving its citizens with no choice in using financial services other than commercial banks. Under such a scenario losers will be people who will be facing monopoly of commercial banks in financial services industry.

Page 14

For example, PEARLS requires a minimum level of operating profit to contribute to the creation of healthy balance sheet reserves. Is it acceptable to for such a result to be achieved by consistently charging interest rates on loans two to three times the market rate? ... Will it be acceptable for the model credit union to behave in a manner contrary to generally accepted standards of credit union operation even if it satisfactorily achieves the PEARLS outcomes?

Although project staff agrees that RCU most likely could reduce their interest rates for loans slightly, the above statement gives wrong message to the reader and does not consider RCU operations in the context of local economic conditions. RCU is charging 48% for unsecured consumer loans per year. Average weighted interest rate on short term 100% secured commercial loans at the end of first quarter of 1996 in commercial banking sector was 33.1%¹. As for the market rates for consumer loans they do not exist, because RCU is the only financial institution consistently providing such loans. Exception, of course, are pawn shops, which charge 190%+ for their consumer loans. Another reason for maintaining relatively high interest rates is a need to build up statutory capital according to the requirements of current Law on Credit Institutions. RCU is putting emphasis in increasing institutional capital instead of share capital, since share nominal is determined only 5 Lats.

¹ Monetary Review #1 1996, Bank of Latvia

COMMENTS ON MID-TERM EVALUATION REPORT WOCCU Lithuania Staff

7/24/96

The general opinion expressed by our staff is that evaluation was carried out on a very high professional level and all observations made in the Mid-term Evaluation draft are very valuable for our future strategies.

Regarding the inadequacy in the project planned time frames:

- * A shortfall of one appointment in local project staff was really a big problem from the project management point, but it is naturally understandable that it took time to organize competition for the applicants and etc. But at the moment staff personnel is completed.
- * Not all planned internships to Poland have been undertaken because of general opinion to organize internships for credit unions people only after few months of CU operation start and after achieving certain results. For this year planned internships will be organized because all operating credit unions will have some experience and CU people will be better prepared for training. Project staff will also have more experience in credit union development process, and internships for them will be more important when they will face Lithuanian credit union movement's problems and will be in the process of the solutions search.
- * The growth of credit union number is linked with general situation on financial market, and unstable positions of major commercial banks as well as their bankruptcies destroyed people confidence to any financial institution. Also people lost their savings and because of very low incomes they are very short in financial sources to start their own financial institution such as credit union. At the moment we have six operating credit unions and we are in the process to start four new credit unions.

We see real chances to organize even more CU as it was planned for the period October 1995-September 1996. (It was planned to organize four to seven new credit unions -or in other words one every two months).

Training:

- * Up till now we have no access to European countries training facilities and to their training materials. At the moment we have already established contacts with International Co-operative College and they provided us with their training programmes. In the future College specialists could assist us with implementation of their training methods and programmes.
- * Polish Credit Union Movement's experience we hope will be very valuable for our training officers and we wish that during their internship to Poland they will have a chance to visit

officers and we wish that during their internship to Poland they will have a chance to visit Polish CU Training Center.

* Together with Latvian Project staff we already started plan our internships to US, Poland. Each of us already identified our training needs according current and potential credit unions needs. Especially new and more deep knowledge of financial management, strategic planning, and services development will be indispensable when we will start training courses for CU managers and financial officers and when credit unions will be faced with specific problems and will need specific consultations from our side.

Model Credit Union:

To choose the right place for Model Credit Union from our point of view is a very crucial step and we anticipate from all existing credit unions to choose the most interested and potentially most advanced CU located in a convenient place with highly trained staff. At the moment is too early to identify which of existing CU will achieve the best results. It will be more beneficial to decide which credit union is the most reliable after some time when certain results will be achieved.

Comments regarding the computerization issues (Vytautas Latinis)

Credit Union Operational Support

With the growth of number of operating Credit Unions it is evident to have a permanent operational support to new born credit union. From this point I can fully agree with the Evaluation Report's recommendation to have maximized availability for project staff to fulfil support service delivery role. Briefly, at it was marked in the Report, this role may be generally considered as being equivalent to that of a "field worker" in the early stage of development of a Credit Union system. Consequently, the project staff should be able to assist in the practical realities of CU governance, management and operations. Further training for the project staff should be organized taking into consideration what is mentioned above.

Additionally, it seems logical to have a strong training center for Credit Union managers and staff to obtain skills in financial management and accounting, loan procedures, Board governance functions, investment risk analysis. The project staff, as well as invited qualified specialists (from banks, for example), should be able to carry out training sessions for credit union personnel.

Regarding computerization strategy. The Evaluation Report stressed the necessity to investigate the common benchmarks for determining the need for computerization of a Credit Union. It was recommended to maintain the operations on a manual system until the agreed upon benchmarks for computerization have been reached. This approach is valuable and we are partially following it. The reason to have some credit unions operating on manual recording system is twofold. First, to gain competence in correctly maintaining an up-to-date manual system, and to learn to identify any error in accounting. Second, while there is a lack

of highly qualified and trained specialists for computer based accounting system for each CU as well as the lack of a software support center, it is better to have a manual system (especially for credit unions located far away from major towns).

However, it is much more complicated to switch to a computer accounting system when the volume of accumulated financial data is huge. Also auditing and external control procedures are more complicated in this case.